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26 July, 1985

MEMORANDUM FOR: Bill Helkie

Board of Governors of the Federal Reserve

SUBJECT : Estimated Impact of a \$5 a barrel tax on oil imports

FROM :

European Issues Division, EURA

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Per your request of 26 July 1985, I simulated the Linked Policy Impact Model to estimate the impact on the United States of a \$5 a barrel tax on imported petroleum. I did the scenario four ways. First, using a baseline forecast in which world oil prices do not fall from an estimated average 1985 price of \$28, a \$5 tax would cut estimated US real GNP by -0.1 percent in 1986, raise inflation by 0.3 percent, and lower the US federal government deficit by \$11 billion.

In the second set of simulations I assumed that the world oil price falls to \$20 a barrel in 1986. This price, compared to the \$28 price would boost US GNP by 0.6 percent and cut US inflation by 1 percentage point. The US federal deficit would fall by \$9 billion.

If, while world oil prices were falling \$8 barrel, the United States imposed a \$5 a barrel tax on imported oil, US GNP would still be higher than with \$28 a barrel, but only 0.5 percent higher rather than 0.6 percent. The federal deficit would be \$21 billion lower than in the baseline scenario with \$28 oil.

In the last scenario, which like Scenario 1 assumes world oil prices stay at \$28, I assume that domestic oil producers are able to push up their prices by the full \$5 a barrel. In Scenario 1, the price of domestically produced oil is assumed not to rise at all. This new assumption raises the impact on real GNP significantly.

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Estimated Impact in the United States  
of a \$5 a barrel on Imported Oil

(Changes in 1986 measured from a baseline scenario assuming  
\$28 a barrel oil in 1986)

	Scenario 1 World Oil Prices stay at \$28, \$5 a barrel tax in US	Scenario 2 World Oil Prices fall to \$20, no US tax	Scenario 3 World Oil Prices fall to \$20, \$5 a barrel tax in US	Scenario 4 Like 1, but full price pass through
Real GNP	-0.1 pct	0.6 pct	0.5 pct	-0.4 pct
Inflation rate	0.3 pct pts	-1.0 pct pts	-0.7 pct pts	1.0 pct pts
Current account deficit	-\$1.0 bill.	-\$12.2 bill.	-\$13.4 bill.	-1.4 bill.
Oil tax revenue	\$10.7 bill.	none	\$10.8 bill.	\$10.9 bill..
Federal Govt. deficit	-\$11.3 bill.	-\$9.4 bill.	-\$20.7 bill	-\$8.6 bill.
Average Energy prices	3.0 pct	-12.7 pct	-9.7 pct	11.0 pct
Oil imports (level, not changes)	5.9 mbd	6.0 mbd	5.9 mbd	5.9 mbd

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